

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition :
of :
The Custom Shop Rector Street Corporation :
for Redetermination of a Deficiency or Revision :
of a Determination or Refund of Corporation :
Franchise Tax under Article 9A of the Tax Law for :
the Periods Ending 7/31/79 - 7/31/81. :
:

AFFIDAVIT OF MAILING

State of New York :

ss.:

County of Albany :

David Parchuck, being duly sworn, deposes and says that he is an employee of the State Tax Commission, that he is over 18 years of age, and that on the 10th day of July, 1985, he served the within notice of Decision by certified mail upon The Custom Shop Rector Street Corporation, the petitioner in the within proceeding, by enclosing a true copy thereof in a securely sealed postpaid wrapper addressed as follows:

The Custom Shop Rector Street Corporation
Attn: J. Nettis, Controller
402-412 Route 23
Franklin, NJ 07416

and by depositing same enclosed in a postpaid properly addressed wrapper in a post office under the exclusive care and custody of the United States Postal Service within the State of New York.

That deponent further says that the said addressee is the petitioner herein and that the address set forth on said wrapper is the last known address of the petitioner.

Sworn to before me this
10th day of July, 1985.

David Parchuck

James A. DeAngelis
Authorized to administer oaths
pursuant to Tax Law section 174

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition :
of :
The Custom Shop Rector Street Corporation :
for Redetermination of a Deficiency or Revision :
of a Determination or Refund of Corporation :
Franchise Tax under Article 9A of the Tax Law for :
the Periods Ending 7/31/79 - 7/31/81. :
:

AFFIDAVIT OF MAILING

State of New York :

ss.:

County of Albany :

David Parchuck, being duly sworn, deposes and says that he is an employee of the State Tax Commission, that he is over 18 years of age, and that on the 10th day of July, 1985, he served the within notice of Decision by certified mail upon Bernard Segal, the representative of the petitioner in the within proceeding, by enclosing a true copy thereof in a securely sealed postpaid wrapper addressed as follows:

Bernard Segal
540 Madison Ave.
New York, NY 10022

and by depositing same enclosed in a postpaid properly addressed wrapper in a post office under the exclusive care and custody of the United States Postal Service within the State of New York.

That deponent further says that the said addressee is the representative of the petitioner herein and that the address set forth on said wrapper is the last known address of the representative of the petitioner.

Sworn to before me this
10th day of July, 1985.

David Parchuck

James A. Hagmann

Authorized to administer oaths
pursuant to Tax Law section 174

STATE OF NEW YORK
STATE TAX COMMISSION
ALBANY, NEW YORK 12227

July 10, 1985

The Custom Shop Rector Street Corporation
Attn: J. Nettis, Controller
402-412 Route 23
Franklin, NJ 07416

Gentlemen:

Please take notice of the Decision of the State Tax Commission enclosed herewith.

You have now exhausted your right of review at the administrative level. Pursuant to section(s) 1090 of the Tax Law, a proceeding in court to review an adverse decision by the State Tax Commission may be instituted only under Article 78 of the Civil Practice Law and Rules, and must be commenced in the Supreme Court of the State of New York, Albany County, within 4 months from the date of this notice.

Inquiries concerning the computation of tax due or refund allowed in accordance with this decision may be addressed to:

NYS Dept. Taxation and Finance
Law Bureau - Litigation Unit
Building #9, State Campus
Albany, New York 12227
Phone # (518) 457-2070

Very truly yours,

STATE TAX COMMISSION

cc: Petitioner's Representative
Bernard Segal
540 Madison Ave.
New York, NY 10022
Taxing Bureau's Representative

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition	:	
of	:	
THE CUSTOM SHOP RECTOR STREET CORPORATION	:	DECISION
for Redetermination of a Deficiency or for	:	
Refund of Corporation Franchise Tax under	:	
Article 9-A of the Tax Law for the Periods	:	
Ending July 31, 1979 through July 31, 1981.	:	

Petitioner, The Custom Shop Rector Street Corporation, 402-412 Route 23, Franklin, New Jersey 07416, filed a petition for redetermination of a deficiency or for refund of corporation franchise tax under Article 9-A of the Tax Law for the periods ending July 31, 1979 through July 31, 1981 (File Nos. 40028 and 42453).

A formal hearing was held before Arthur Bray, Hearing Officer, at the offices of the State Tax Commission, Two World Trade Center, New York, New York, on November 1, 1984 at 9:30 A.M., with all briefs to be submitted on or before December 7, 1984. Petitioner appeared by Bernard Segal, Esq. The Audit Division appeared by John P. Dugan, Esq. (Anna Colello, Esq., of counsel).

ISSUE

Whether income received by petitioner from an affiliated company, where such income was generated by investment of petitioner's excess cash by such affiliate of petitioner, constituted business income from business capital or investment income from investment capital under Article 9-A of the Tax Law.

FINDINGS OF FACT

1. Petitioner, The Custom Shop Rector Street Corporation, is a retail firm which engages in the sale of shirts.

2. Petitioner filed a State of New York Corporation Franchise Tax Report for the periods ended July 31, 1979, July 31, 1980 and July 31, 1981. On each of these reports, petitioner reported on its schedule of investment capital, investments which were allocated to petitioner by an affiliated corporation known as The Custom Shop Payment Corp. ("Payment Corp."). Petitioner also claimed a fifty percent dividend deduction based upon the dividends allocated to it from Payment Corp.

3. The Audit Division issued notices of deficiency to petitioner asserting deficiencies of corporation franchise tax under Article 9-A of the Tax Law as follows:

<u>Date of Notice</u>	<u>Period Ending</u>	<u>Additional Tax Asserted to be Due</u>	<u>Interest</u>	<u>Amount Asserted to be Due</u>	<u>Amount Paid or Credit</u>	<u>Balance</u>
8/11/82	7/31/79	\$2,381.18	\$ 783.65	\$3,164.83	\$ -0-	\$3,164.83
12/22/83	7/31/80	3,891.00	1,601.54	5,492.54	2,514.00	2,978.54
1/5/83	7/31/81	5,649.00	1,202.39	6,851.39	-0-	6,851.39

4. Each of the asserted deficiencies of corporation franchise tax were based on the Audit Division's conclusion that certain income received by petitioner should be considered business income from business capital rather than investment income from investment capital. For the fiscal years ended July 31, 1980 and July 31, 1981, the asserted deficiencies were also premised upon the disallowance of the fifty percent dividend deduction on the basis that petitioner was not the owner of the stock to which the dividends were attributable. After the Notice of Deficiency for the fiscal year ended July 31, 1979 was issued, the Audit Division increased the amount of the asserted deficiency of tax from \$2,381.18 to \$2,890.56 pursuant to section 1089(d) of the Tax Law on the basis of the disallowance of the fifty percent dividend deduction.

5. Petitioner is one of approximately fifty separate affiliated corporations engaged in retail clothing sales. Over time, petitioner and its sister corporations

acquired excess funds. Accordingly, the decision was made to establish a central corporation, which became known as Payment Corp., to accumulate funds from each of the retail corporations in order to have all of the excess funds managed by an individual with expertise in investments.

6. On approximately a weekly basis, petitioner sends its excess funds, by check, to Payment Corp. Petitioner records the funds sent to Payment Corp. on its balance sheet as "other investments". Payment Corp., in turn, reflects the funds it receives on its financial statement as investments for others and not as loans. There are no documents executed by petitioner and Payment Corp. evidencing a loan.

7. Payment Corp. invests the funds it receives in such items as stock, certificates of deposit, money market funds and treasury bills. The type of investment is based upon Payment Corp.'s judgment as to which investments are preferable.

8. All of the stocks, bonds and certificates of deposit are registered in the name of Payment Corp. in order to facilitate the sale of securities. Petitioner makes no direct investments of its own.

9. Payment Corp. allocates its investments to petitioner as well as petitioner's sister corporations on the basis of the sales of a particular retail operation to all retail operations. The profits, dividends, capital gains and interest are reported on the tax returns of the separate retail corporations and not on the tax returns of Payment Corp.

CONCLUSIONS OF LAW

A. That subdivision 5 of section 208 of the Tax Law provides, in part:

"The term 'investment capital' means investments in stocks, bonds and other securities, corporate and governmental, not held for sale to customers in the regular course of business, exclusive of subsidiary capital and stock issued by the taxpayer..."

B. That 20 NYCRR 3-4.2(a) provides, in part:

"The term 'investment capital' means the total of the average fair market value of the taxpayer's investments in stocks, bonds and other securities issued by any corporation (other than the taxpayer, a subsidiary or a DISC) or by the United States, any state, territory or possession of the United States, the District of Columbia, or any foreign country, or any political subdivision or governmental instrumentality of any of the foregoing." (emphasis added).

C. That since the investments were in the name of Payment Corp. and not petitioner, the Audit Division properly concluded that they were not "the taxpayer's investments" within the meaning of 20 NYCRR 3-4.2(a). Accordingly, the investments were properly considered business capital (Tax Law §208.7). It is noted that the situation presented herein is not analogous to an investment in a mutual fund inasmuch as the return on the investment is based on relative sales volume and not the relative amount invested.

D. That since petitioner did not own the stocks to which the dividends were attributable, petitioner was not entitled to the fifty percent dividend deduction which was taken pursuant to Tax Law section 208.9 (subd. [a], par. [2]).

E. That the petition of The Custom Shop Rector Street Corporation is denied and the notices of deficiency, as modified (see Finding of Fact "4"), are sustained.

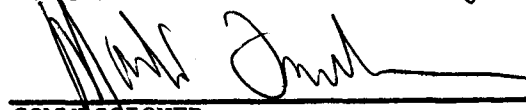
DATED: Albany, New York

STATE TAX COMMISSION

JUL 10 1985


PRESIDENT


COMMISSIONER


COMMISSIONER